

PROSPECTS AS BRIGHT AS EVER

Gold - the innocent bystander to the hurricane

A leading US precious metals analyst predicts gold will jump back as fast as it has come down and reach \$1,000 again this year or early next - and perhaps \$2,000 in the next few years.

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LONDON -

Gold is still lingering around the \$780 mark, but many analysts predict that this will not continue with fundamentals set to drive prices higher once the current financial meltdown steadies - although how long this will take is the major uncertainty.

I am indebted to Jeffrey Nichols of American Precious Metals Advisors for the following quote: "...gold's swift descent in the past few weeks is a direct consequence of the unfolding global credit crisis. In short, gold has been an innocent bystander to the financial hurricane hitting Wall Street and global markets"

The past few months have seen a huge fall in the gold price from its brief plus thousand dollar peak. Latterly, gold followed the oil price downwards and on some days one could have virtually superimposed a gold price graph over the top of the oil price one and it would have been tough to tell the difference.

This led to comments that the oil and gold prices were inescapably linked and for several weeks this indeed seemed to be the position. Memories are short though as the gold price hadn't followed oil up to its July peak. Mineweb commented in July - just a few days before oil started its price correction - that the oil price looked overcooked and suggested that oil at \$90 and gold at \$900 might be something we could see shortly. Well, at least we were half right! But, as noted above gold came back virtually pari-passu with oil and ploughed well below the \$900 mark, right back to around \$750, but at this kind of level has seen huge physical demand resurrected in the Middle and Far East - and even in the USA - as consumers believe that gold is a bargain at these kinds of levels.

But, it may have taken the Lehman collapse to begin to see the inevitable decoupling of the gold price trend from that of the oil price with the latter continuing to fall - below \$90 at one stage - but gold making at least a small recovery.

Overall though there does seem to be a major dichotomy in the way gold has been behaving. The past few weeks have seen enormous physical demand reported as some 300 percent above the same time last year in some traditional gold trading areas, yet the metal price has remained weak, well below the \$800 level.

Of course the problem for the market is gold held by big investment funds and in ETFs which, in a financial crisis such as that we are seeing at the current time, does not necessarily behave the way one would expect it to. Gold is considered to be a 'safe haven' protecting the investor against the kind of market meltdown we are currently seeing. However the need for liquidity, as the crisis is so severe for some investors, is such that precious metals holdings are being sold to cover this which, in turn, has put additional downward pressure on the price.

Nichols puts this as follows: "The yellow metal's own positive fundamentals - and even its role as a safe haven in turbulent financial seas - have simply been overwhelmed by the massive storm-surge flight to cash and the indiscriminate selling of securities and commodities, selling that has been amplified and accelerated by automatic program trading, short covering, and technical triggers on the way down."

As financial turmoil continues there may be more liquidation of inflation protecting assets like gold, but at some stage logic tells us that this should cease with the metal's strong fundamentals coming to the fore. A key player here will be the US dollar with gold tending to move in the opposite direction to the perceived value of the US currency. At some stage the current better value perception of the dollar has to reverse yet again as the US economy remains in serious trouble with the continuation of the country's huge deficit which continues to trend upwards. If the Fed - as some believe - is forced into cutting rates again, Nicholls feels this could be the trigger which could see the dollar dive again and gold recover strongly.

Global inflation, too, seems to be accelerating which is likely to be another stimulus for an increase in the gold price. So with physical demand running high, inflation rising, gold production static or falling, leading economies in disarray, or even in crisis, all the factors favoring a gold price increase would seem to be in place.

Nichols comments: "Long-term price prospects remain as bright as ever -- and nothing in the recent market performance has changed our forecast of record high prices in the next few years: We still expect to see gold back over \$1,000, if not late this year, then almost certainly in the first quarter of 2009. With the right confluence of economic and geopolitical developments we could see gold as high as \$1,500 or even \$2,000 an ounce in the next few years -- and a buying frenzy, such as is often seen late in the price cycles of financial and commodity markets, could briefly take the metal much higher."

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